

REPORT BY THE
AUDITOR GENERAL
OF CALIFORNIA

**FINANCIAL AUDIT REPORT
CALIFORNIA STUDENT AID COMMISSION
STATE GUARANTEED STUDENT LOAN PROGRAM
YEAR ENDED JUNE 30, 1982**

REPORT BY THE
OFFICE OF THE AUDITOR GENERAL
TO THE
JOINT LEGISLATIVE AUDIT COMMITTEE

F-243

FINANCIAL AUDIT REPORT
CALIFORNIA STUDENT AID COMMISSION
STATE GUARANTEED STUDENT LOAN PROGRAM
YEAR ENDED JUNE 30, 1982

MAY 1983



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May 12, 1983

F-243

Honorable Art Agnos
Chairman, and Members of the
Joint Legislative Audit Committee
State Capitol, Room 3151
Sacramento, California 95814

Dear Mr. Chairman and Members:

The Office of the Auditor General presents its report concerning a fiscal audit of the California Student Aid Commission State Guaranteed Student Loan Program for the year ended June 30, 1982.

Respectfully submitted,

Thomas W. Hayes
THOMAS W. HAYES
Auditor General

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INTRODUCTION

We have conducted a financial audit of the California Student Aid Commission's State Guaranteed Student Loan Program. The California Student Aid Commission (commission) requested this audit to meet its obligation to provide audited financial statements to lenders participating in this loan program. The Office of the Auditor General also conducted a performance audit of the State Guaranteed Student Loan Program as well as other programs of the commission. Our April 1982 report entitled "A Review of the Student Aid Commission's Administration of Major Student Aid Programs" (Report No. P-015), presents the results of this performance audit.

Chapter 1201, Statutes of 1977, established the State Guaranteed Student Loan Program and authorized the California Student Aid Commission to serve as a guarantee agency for student loans. This program carries out the provisions of the Federal Guaranteed Student Loan Program instituted within the Federal Higher Education Act of 1965, as amended (Education Code, Section 69760). The commission is responsible for guaranteeing federally reinsured loans that are issued to eligible students.

The commission has contracted with United Student Aid Funds, Inc., a nonprofit corporation, for administrative support services. These services include processing and approving all student loan applications, managing guaranteed loans, processing claims from lenders, and preparing reports required by the United States Office of Education.

The State Guaranteed Student Loan Program is supported primarily by federal funds, investment earnings, and insurance premiums paid by student borrowers.

We conducted the present audit under the authority vested in the Auditor General by Section 10500 et seq. of the Government Code.

AUDITOR'S OPINION

We have examined the balance sheets of the California Student Aid Commission's State Guaranteed Student Loan Program as of June 30, 1981, and 1982, and the related statements of revenues, expenditures, and changes in fund balance for the years then ended. Our examination was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of the California Student Aid Commission's State Guaranteed Student Loan Program at June 30, 1981, and 1982, and the results of operations and changes in fund balance for the years then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding years.

OFFICE OF THE AUDITOR GENERAL



By: KARL W. DOLK, CPA
Assistant Auditor General

Date: December 6, 1982

Staff: Curt Davis, CPA, Audit Manager
Enrique Farias, CPA
Dorie Harmon, CPA
Sylvia Hensley

**CALIFORNIA STUDENT AID COMMISSION
STATE GUARANTEED STUDENT LOAN PROGRAM
COMPARATIVE BALANCE SHEET AS OF JUNE 30**

ASSETS

	<u>1981</u>	<u>1982</u>
Cash	\$ 10,669	\$ 44,249
Accounts receivable (Note 2)	258,358	344,793
Due from other funds (Note 3)	13,594,993	29,209,308
Due from other governments (Note 4)	2,622,564	5,687,317
Equipment	<u>50,207</u>	<u>83,348</u>
 Total Assets	 <u>\$16,536,791</u>	 <u>\$35,369,015</u>

LIABILITIES AND FUND EQUITY

Liabilities:		
Due to other funds (Note 5)	<u>\$ 1,154,883</u>	<u>\$ 1,271,276</u>
 Total Liabilities	 <u>1,154,883</u>	 <u>1,271,276</u>
 Fund Equity:		
Investment in fixed assets	<u>50,207</u>	<u>83,348</u>
 Fund Balance:		
Reserved for loan defaults (Note 6)	9,920,941	22,771,788
Designated for federal advance (Note 7)	2,150,153	2,144,764
Undesignated	<u>3,260,607</u>	<u>9,097,839</u>
 Total Fund Balance	 <u>15,331,701</u>	 <u>34,014,391</u>
 Total Fund Equity	 <u>15,381,908</u>	 <u>34,097,739</u>
 Total Liabilities and Fund Equity	 <u>\$16,536,791</u>	 <u>\$35,369,015</u>

The notes to the financial statements are an integral part of this statement.

**CALIFORNIA STUDENT AID COMMISSION
STATE GUARANTEED STUDENT LOAN PROGRAM
COMPARATIVE STATEMENT OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCE
FOR FISCAL YEARS ENDING JUNE 30**

	<u>1981</u>	<u>1982</u>
Revenues:		
Insurance premiums (Note 9)	\$ 9,492,185	\$16,063,559
Intergovernmental revenue (Note 4)	2,888,449	5,737,317
Interest	909,313	2,531,342
Miscellaneous income	<u>153,364</u>	<u>6,044</u>
Total Revenues	<u>13,443,311</u>	<u>24,338,262</u>
Expenditures:		
Personal services	508,016	690,341
Operating expenses and equipment	379,745	310,659
Contract fees (Note 11)	<u>1,881,869</u>	<u>4,654,572</u>
Total Expenditures	<u>2,769,630</u>	<u>5,655,572</u>
Excess of Revenues Over Expenditures	10,673,681	18,682,690
Fund balance July 1	<u>4,658,020</u>	<u>15,331,701</u>
Fund balance June 30	<u>\$15,331,701</u>	<u>\$34,014,391</u>

The notes to the financial statements are an integral part of this statement.

CALIFORNIA STUDENT AID COMMISSION
STATE GUARANTEED STUDENT LOAN PROGRAM
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 1982

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements reflect the financial position and results of operations of the State Guaranteed Student Loan Program of the California Student Aid Commission (commission). The financial statements have been prepared in conformity with generally accepted accounting principles applicable to state and local governments as prescribed by the American Institute of Certified Public Accountants and by the National Council on Governmental Accounting. Below is a summary of the more significant accounting policies.

Fund Accounting

The State Guaranteed Student Loan Program is accounted for separately as a part of the State Guaranteed Loan Reserve Fund. The State Guaranteed Loan Reserve Fund was created to account for all monies received for guaranteeing loans to college students and to account for reimbursements to lending institutions for defaulted student loans. This fund is accounted for as an Expendable Trust Fund. Expendable Trust Funds are used to account for assets held by the governmental unit as a trustee or as an agent for individuals, private organizations, other governmental units, and other funds.

Basis of Accounting

Expendable Trust Funds are accounted for on a modified accrual basis of accounting. Revenues are recognized in the accounting period in which they become measurable and available. Expenditures are recognized, if measurable, in the accounting period in which the liability is incurred.

Vacation and Sick Leave

Costs of vacation and sick leave are charged at the time these benefits are used rather than when they are earned.

2. ACCOUNTS RECEIVABLE

This account represents insurance premiums collected by United Student Aid Funds, Inc., during June 1981, and 1982. The commission received the premium payments from this corporation in July 1981 and 1982, respectively.

3. DUE FROM OTHER FUNDS

This account includes amounts due from the Surplus Money Investment Fund (SMIF) for temporary cash investments and interest earned on the investments and amounts due from the General Fund for insurance premiums collected by the General Fund but not remitted to the State Guaranteed Loan Reserve Fund as of June 30.

<u>Fund</u>	<u>1981</u>	<u>1982</u>
SMIF Investment	\$12,414,000	\$27,207,000
SMIF Interest	<u>563,494</u>	<u>1,538,535</u>
Total SMIF	12,977,494	28,745,535
General Fund	<u>617,499</u>	<u>463,773</u>
Total	<u>\$13,594,993</u>	<u>\$29,209,308</u>

4. DUE FROM OTHER GOVERNMENTS

This account represents the June 30, 1981, and 1982, balances due from the United States Secretary of Education for the amounts billed for reimbursement of administrative costs. The amounts apply to administrative costs that were incurred between July 1 and June 30 of the respective fiscal years, and that are due in the subsequent fiscal years. Under present procedures, the commission bills the United States Secretary of Education for reimbursement of one percent of the balance of loans guaranteed or actual administrative costs, whichever is less. Whether the Secretary of Education pays the invoice depends upon the availability of federal funds.

5. DUE TO OTHER FUNDS

This account represents those operating costs incurred by the General Fund on behalf of the State Guaranteed Student Loan Reserve Fund during June 1981 and 1982, respectively.

6. RESERVED FOR LOAN DEFAULTS

The commission must maintain a reserve for the repurchase of defaulted loans. The commission is required initially to deposit at least 80 percent of the cumulative insurance premium revenue to this reserve. These funds can be used only for the purchase of defaulted loans. Total insurance premiums collected were \$12,401,176 and \$28,464,735 as of June 30, 1981, and June 30, 1982, respectively.

7. DESIGNATED FOR FEDERAL ADVANCE

Before 1967, the United States Secretary of Education advanced \$1,479,865 to the commission for the Guaranteed Loan Program, which existed at the time; the Guaranteed Loan Program is referred to as the "old program." The commission received other advances totaling \$1,129,211 for the revised loan program. The revised loan program, titled the State Guaranteed Student Loan Program, was enacted in 1977 and is referred to as the "new program." These advances were made under an agreement between the United States Secretary of Education and the commission. In part, this agreement states as follows:

The Secretary may call upon the Agency for repayment of part or all of any sums advanced to the Agency hereunder, at such times and to the extent that he determines, in the light of the maturity and solvency of the Fund and after taking into account the Agency's requirements for its then outstanding obligations as well as its requirements for future loans and commitments based on its prior performance and established trends, that to do so will best carry out the purposes of the Act.

Although reported separately, the programs are accounted for in the State Guaranteed Loan Reserve Fund. As of June 30, 1982, the "old program" fund balance was \$464,312. Consequently, the remaining advance balance of \$2,144,764 could be payable from the State Guaranteed Student Loan Program fund balance as of June 30, 1982.

8. LENDERS' AGREEMENTS

The commission's agreements with lending institutions require that it maintain a Guarantee Reserve Fund. This fund must be represented by cash and marketable securities having a market value of not less than one percent of the total amount of unpaid principal and interest of all approved notes that are covered by federal reinsurance under the agreement between the commission and the United States Secretary of Education. At June 30, 1981, and 1982, the commission's cash and marketable securities exceeded the amounts required.

9. INSURANCE PREMIUMS

Student borrowers pay insurance premiums when their loans are disbursed by the lending institution. The commission may use the premiums to underwrite defaulted loans and to cover costs that the commission incurs in administering the loan program.

10. RETIREMENT COMMITMENTS

Regular employees of the commission are members of the Public Employees' Retirement System (PERS), which is a defined benefit, contributory retirement plan. The amount that the commission and its employees contribute to the PERS is actuarially determined under a program in which contributions plus retirement system earnings provide the necessary funds to pay retirement costs as they are accrued. The State Guaranteed Student Loan Program's share of retirement contributions were \$56,001 and \$78,765 for fiscal years 1980-81 and 1981-82, respectively.

11. CONTRACT FEES

This figure represents amounts paid to United Student Aid Funds, Inc., for administrative support services. The fees are calculated as a percentage of the total amount of loans outstanding at the end of each month.

12. SUBSEQUENT EVENTS

The contract for administrative support services for the loan program has been awarded to Electronic Data Systems Corporation for the period from January 3, 1983, to February 28, 1986. Between July 1, 1982, and January 31, 1983, United Student Aid Funds, Inc., continued to provide services under a contract amendment.

13. FEDERAL REINSURANCE AGREEMENT

The agreements between the California Student Aid Commission and the lenders participating in the loan program require that the commission purchase guaranteed loans that have been defaulted if the lender has exercised due diligence in making, servicing, and collecting the loan. Likewise, the agreement between the commission and the United States Secretary of Education requires the Secretary of Education to purchase a percentage of those defaulted loans purchased by the commission. Through federal fiscal year 1982-83, the Secretary of Education will purchase 100 percent of the defaulted loans. For federal fiscal year 1983-84 and after, the percentage of defaulted loans purchased by the Secretary of Education may decrease depending upon the default rate of the State Guaranteed Student Loan Program.

OTHER COMMENTS

As an integral part of our examination, we reviewed the accounting procedures of the California Student Aid Commission (commission) and its related system of internal accounting control to the extent we considered necessary to properly form an opinion concerning the fairness with which the State Guaranteed Student Loan Program's financial statements present the program's financial position and the results of operations in accordance with generally accepted accounting principles consistently applied. As part of our review, we issued a management letter to the commission suggesting action that it should take to assure that it receives the funds it is entitled to. Our letter also recommended adjusting entries necessary to achieve compliance with generally accepted accounting principles. The commission is taking action to assure that it receives the funds it is entitled to and concurs with the adjusting entries.

cc: Members of the Legislature
Office of the Governor
Office of the Lieutenant Governor
State Controller
Legislative Analyst
Director of Finance
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
Capitol Press Corps